

Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended and P.A. 71 of 1919, as amended.

Local Unit of Government Type <input type="checkbox"/> County <input type="checkbox"/> City <input type="checkbox"/> Twp <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other				Local Unit Name Pellston Public Schools		County Emmet	
Fiscal Year End June 30, 2006		Opinion Date July 21, 2006		Date Audit Report Submitted to State October 4, 2006			

We affirm that:

We are certified public accountants licensed to practice in Michigan.

We further affirm the following material, "no" responses have been disclosed in the financial statements, including the notes, or in the Management Letter (report of comments and recommendations).

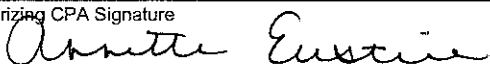
YES NO

Check each applicable box below. (See instructions for further detail.)

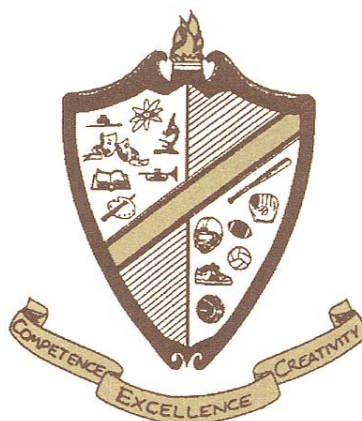
1. ☒ ☐ All required component units/funds/agencies of the local unit are included in the financial statements and/or disclosed in the reporting entity notes to the financial statements as necessary.
2. ☒ ☐ There are no accumulated deficits in one or more of this unit's unreserved fund balances/unrestricted net assets (P.A. 275 of 1980) or the local unit has not exceeded its budget for expenditures.
3. ☒ ☐ The local unit is in compliance with the Uniform Chart of Accounts issued by the Department of Treasury.
4. ☒ ☐ The local unit has adopted a budget for all required funds.
5. ☒ ☐ A public hearing on the budget was held in accordance with State statute.
6. ☒ ☐ The local unit has not violated the Municipal Finance Act, an order issued under the Emergency Municipal Loan Act, or other guidance as issued by the Local Audit and Finance Division.
7. ☒ ☐ The local unit has not been delinquent in distributing tax revenues that were collected for another taxing unit.
8. ☒ ☐ The local unit only holds deposits/investments that comply with statutory requirements.
9. ☒ ☐ The local unit has no illegal or unauthorized expenditures that came to our attention as defined in the *Bulletin for Audits of Local Units of Government in Michigan*, as revised (see Appendix H of Bulletin).
10. ☒ ☐ There are no indications of defalcation, fraud or embezzlement, which came to our attention during the course of our audit that have not been previously communicated to the Local Audit and Finance Division (LAFD). If there is such activity that has not been communicated, please submit a separate report under separate cover.
11. ☒ ☐ The local unit is free of repeated comments from previous years.
12. ☒ ☐ The audit opinion is UNQUALIFIED.
13. ☒ ☐ The local unit has complied with GASB 34 or GASB 34 as modified by MCGAA Statement #7 and other generally accepted accounting principles (GAAP).
14. ☒ ☐ The board or council approves all invoices prior to payment as required by charter or statute.
15. ☒ ☐ To our knowledge, bank reconciliations that were reviewed were performed timely.

If a local unit of government (authorities and commissions included) is operating within the boundaries of the audited entity and is not included in this or any other audit report, nor do they obtain a stand-alone audit, please enclose the name(s), address(es), and a description(s) of the authority and/or commission.

I, the undersigned, certify that this statement is complete and accurate in all respects.

We have enclosed the following:		Enclosed	Not Required (enter a brief justification)	
Financial Statements		<input checked="" type="checkbox"/>		
The letter of Comments and Recommendations		<input checked="" type="checkbox"/>		
Other (Describe)		<input type="checkbox"/>		
Certified Public Accountant (Firm Name) Rehmann Robson			Telephone Number 231-627-3143	
Street Address 902 S. Huron Street, PO Box 250			City Cheboygan	State MI
Zip 49721				
Authorizing CPA Signature 		Printed Name Annette M Eustice, CPA, CGFM		License Number 1101019667

PELLSTON PUBLIC SCHOOLS



FINANCIAL STATEMENTS

FOR THE YEAR ENDED JUNE 30, 2006

PELLSTON PUBLIC SCHOOLS
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INDEPENDENT AUDITORS' REPORT

July 21, 2006

Board of Education
Pellston Public Schools
Pellston, Michigan

We have audited the accompanying financial statements of the governmental activities, each major fund and the aggregate remaining fund information of **Pellston Public Schools**, as of and for the year ended June 30, 2006, which collectively comprise the District's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of **Pellston Public Schools'** management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of **Pellston Public Schools** as of June 30, 2006, and the respective changes in financial position thereof and the budgetary comparisons for the General Fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated July 21, 2006, on our consideration of **Pellston Public Schools'** internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financing reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Management's Discussion and Analysis on pages I–VI is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the **Pellston Public Schools** basic financial statements. The supplementary information in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements of **Pellston Public Schools**. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented, in all material respects, in relation to the basic financial statements taken as a whole.

A handwritten signature in black ink, reading "Lehmann Johnson". The signature is written in a cursive, flowing style with a large initial 'L'.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Management's Discussion and Analysis

As management of the Pellston Public Schools (the "District"), we offer readers of the District's financial statements this narrative overview and analysis of the financial activities of the District for the fiscal year ended June 30, 2006.

Financial Highlights

- The liabilities of the District exceeded its assets at the close of the most recent fiscal year by \$4,761,731 *net assets (deficit)*. Of this amount \$5,423,518 resulted from debt exceeding the capital assets. Unrestricted net assets of \$171,166 may be used to meet the District's ongoing obligations. Net assets of \$490,621 are restricted for debt service.
- The government's total net assets (deficit) increased by \$319,572.
- As of the close of the current fiscal year, the District's governmental funds reported combined ending fund balances of \$785,135, a decrease of \$29,473 in comparison with the prior year.
- At the end of the current fiscal year, unreserved fund balance for the General Fund was \$254,459 or 4.3% percent of total General Fund expenditures.
- The District had no new bonds or notes payable and made principal payments of \$517,202 during the year.
- The District repaid the remaining balance on the 2004 state aid anticipation note of \$1,400,000 and borrowed \$1,500,000 on a 2005 state aid anticipation note.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. The District's basic financial statements comprise three components: 1) District-wide financial statements, 2) fund financial statements and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

District-wide financial statements. The *District-wide financial statements* are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private-sector business.

The *statement of net assets* presents information on all of the District's assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The *statement of activities* presents information showing how the District's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., earned but unused sick or vacation leave).

Both of the District-wide financial statements present activities of the District that are principally supported by taxes and intergovernmental revenues. The governmental activities of the District include instruction, supporting services, food services and athletics. The District had no business-type activities as of and for the year ended June 30, 2006.

The District-wide financial statements can be found on pages 3-4 of this report.

Fund financial statements. A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The District, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the District can be divided into two categories: governmental funds and fiduciary funds.

Governmental funds. *Governmental funds* are used to account for essentially the same functions reported as *governmental activities* in the District-wide financial statements. However, unlike the District-wide financial statements, governmental fund financial statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in evaluating a District's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the District-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the District-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental funds balance sheet and the governmental funds statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

The District maintains 9 individual governmental funds. Information is presented separately in the governmental funds balance sheet and in the governmental funds statement of revenues, expenditures, and changes in fund balances for the General Fund and the 1992 Debt Service Fund, which are considered to be major funds. Data from the other seven governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these nonmajor governmental funds is provided in the form of *combining statements* elsewhere in this report.

The District adopts an annual appropriated budget for its General Fund and each special revenue fund. Budgetary comparison statements have been provided for the General Fund herein to demonstrate compliance with those budgets.

The basic governmental funds financial statements can be found on pages 5-9 of this report.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the District. Fiduciary funds are *not* reflected in the District-wide financial statements because the resources of those funds are *not* available to support the District's own programs.

The basic fiduciary fund financial statement can be found on page 10 of this report.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 11-25 of this report.

Other information. The combining statements referred to earlier in connection with nonmajor governmental funds are presented immediately following the notes to the financial statements. Combining fund statements can be found on pages 26-27 of this report.

District-wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the District, its liabilities exceeded assets by \$4,761,731 at the close of the most recent fiscal year. It is expected that a deficit will continue until such time as debt incurred by the Board of Education for facility improvements between 1993 and 2004 is substantially repaid and the value of the improved facilities is greater than the sum of outstanding bonds for the improvements.

By far the largest portion of the District's net assets (deficit) reflects its investment in capital assets (e.g., land and improvements, buildings and improvements, equipment, and vehicles); less any related debt used to acquire those assets that is still outstanding. The District uses these capital assets to provide services to the students it serves; consequently, these assets are *not* available for future spending. Although the District's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

A portion of the District's net assets (deficit) represents resources that are subject to external restrictions on how they may be used. The District has \$490,621 of net assets restricted for debt service. The remaining balance of \$171,166 is *unrestricted net assets*.

District's Net Assets (Deficit)

	<u>2006</u>	<u>2005</u>
Assets		
Current and other assets	\$ 2,949,235	\$ 1,658,437
Capital assets, net	<u>6,027,797</u>	<u>6,575,845</u>
Total assets	<u>8,977,032</u>	<u>8,234,282</u>
Liabilities		
Current liabilities	2,747,165	1,443,895
Long-term liabilities outstanding	<u>10,991,598</u>	<u>11,232,546</u>
Total liabilities	<u>13,738,763</u>	<u>12,676,441</u>
Net assets		
Invested in capital assets, net of related debt	(5,423,518)	(5,073,775)
Restricted	490,621	467,159
Unrestricted	<u>171,166</u>	<u>164,457</u>
Total net assets (deficit)	<u>\$ (4,761,731)</u>	<u>\$ (4,442,159)</u>

The District's deficit increased by \$319,572 during the current fiscal year. Most of this increase is due to depreciation. The District's blended enrollment is approximately 750 students.

District's Changes in Net Assets (Deficit)

	<u>2006</u>	<u>2005</u>
Revenues		
Program revenues		
Charges for services	\$ 148,520	\$ 151,627
Operating grants and contributions	1,083,732	1,037,142
General revenues		
Property taxes	3,350,540	3,072,215
Grants and contributions not restricted to specific programs	2,669,957	2,731,468
Other	<u>49,131</u>	<u>18,855</u>
Total revenues	<u>7,301,880</u>	<u>7,011,307</u>
Expenses		
Instruction	3,868,186	3,768,785
Supporting services	1,856,144	1,915,545
Food services	256,902	246,251
Athletics	166,680	160,062
Interest on long-term debt	870,290	829,572
Depreciation – unallocated	<u>603,250</u>	<u>606,183</u>
Total expenses	<u>7,621,452</u>	<u>7,526,398</u>
Change in net assets	(319,572)	(515,091)
Net assets (deficit), beginning of year	<u>(4,442,159)</u>	<u>(3,927,068)</u>
Net assets (deficit), end of year	<u>\$ (4,761,731)</u>	<u>\$ (4,442,159)</u>

Financial Analysis of the Government's Funds

As noted earlier, the District uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental funds. The focus of the District's *governmental funds* is to provide information on near-term inflows, outflows, and balances of *spendable* resources. Such information is useful in assessing the District's financing requirements. In particular, *unreserved fund balance* may serve as a useful measure of the District's net resources available for spending at the end of the fiscal year.

As of the end of the current fiscal year, the District's governmental funds reported combined ending fund balances of \$785,135, a decrease of \$29,473 in comparison with the prior year. Approximately 37% of this total amount or \$289,302 constitutes *unreserved fund balance*, which is available for spending at the District's discretion. The remainder of fund balance is *reserved* to indicate that it is not available to fund current expenditures.

The General Fund is the principal operating fund of the District. At the end of the current fiscal year, unreserved fund balance of the General Fund was \$254,459. As a measure of the General Fund's liquidity, it may be useful to compare total fund balance to total fund expenditures. Fund balance represents approximately 4.3% of total General Fund expenditures.

The fund balance of the District's General Fund decreased by \$54,329 during the current fiscal year. This decrease is primarily attributable to wages and fringe benefits for long term substitute teachers to cover for teachers who were on medical leave and unanticipated increases in fuel costs to heat the buildings and to operate the buses.

General Fund Budgetary Highlights

Differences between the original and final amended budgets were relatively minor. As additional information became known during the fiscal year, budget amendments were made to recognize the additional revenue and/or planned expenditures related to various District programs.

Capital Asset and Debt Administration

Capital assets. The District's investment in capital assets as of June 30, 2006, amounted to \$6,027,797 (net of accumulated depreciation). This investment in capital assets includes land and improvements, buildings and improvements, vehicles and equipment.

District's Capital Assets (net of depreciation, when applicable)

Land and improvements	\$ 73,500
Buildings and improvements	5,406,117
Vehicles	343,191
Equipment	<u>204,989</u>
Total	<u>\$ 6,027,797</u>

Additional information on the District's capital assets can be found in Note III C on page 18 of this report.

Long-term debt. At the end of the current fiscal year, the District had total bonded debt, installment contracts, accreted interest on capital appreciation bonds, accrued compensation and retirement payable outstanding of \$11,501,643. Of this amount, \$25,768 are "Durant Bonds" which are not a general obligation of the District and does not constitute an indebtedness of the District within any constitutional or statutory limitations, and is payable solely from the State of Michigan.

The District incurred no new bonds and notes payable and made principal payments of \$517,202 during the year.

Additional information on the District's long-term debt can be found in Note III F on pages 20-22 of this report.

Factors Bearing on the District's Fiscal 2007 Budget

The following factors were considered in preparing the District's budget for the 2006-2007 fiscal year:

- The Board anticipates a slight decrease in pupil membership in fiscal 2007. This decrease, however, will be offset by an anticipated increase in state aid of \$230 per full-time pupil membership.
- With the approval of an additional millage for operations, the District will restore the non-homestead millage to 18 mills.
- Wages are anticipated to increase approximately 2% and fringe benefits increases will be approximately 8%.
- Decreases in spending for personnel, purchased services and supplies are anticipated in fiscal 2007 in order to offset the increases in wages and benefits and the increase in fuel costs anticipated.

Requests for Information

This financial report is designed to provide a general overview of the District's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Pellston Public Schools, Superintendent of Schools, 172 N. Park Street, Pellston, Michigan 49769-0016.

BASIC FINANCIAL STATEMENTS

DISTRICT-WIDE FINANCIAL STATEMENTS

PELLSTON PUBLIC SCHOOLS

STATEMENT OF NET ASSETS

JUNE 30, 2006

	<u>Governmental Activities</u>
Assets	
Current assets	
Cash and cash equivalents	\$ 1,110,616
Investments	1,275,747
Receivables	557,660
Inventory	<u>5,212</u>
Total current assets	2,949,235
Capital assets not being depreciated	35,000
Capital assets being depreciated, net	<u>5,992,797</u>
Total assets	<u>8,977,032</u>
Liabilities	
Current liabilities	
Accounts payable and accrued expenses	693,442
State aid note	1,543,678
Current portion of long-term debt	<u>510,045</u>
Total current liabilities	2,747,165
Noncurrent portion of long-term debt	<u>10,991,598</u>
Total liabilities	<u>13,738,763</u>
Net assets	
Invested in capital assets, net of related debt	(5,423,518)
Restricted for	
Debt service	490,621
Unrestricted	<u>171,166</u>
Total net assets (deficit)	<u><u>\$ (4,761,731)</u></u>

The accompanying notes are an integral part of these financial statements.

PELLSTON PUBLIC SCHOOLS

STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED JUNE 30, 2006

Functions / Programs	Expenses	Program Revenues		Net (Expense) Revenue
		Charges for Services	Operating Grants and Contributions	
Governmental activities				
Instruction	\$ 3,868,186	\$ 4,149	\$ 862,261	\$ (3,001,776)
Supporting services	1,856,144	19,372	40,466	(1,796,306)
Food services	256,902	82,512	181,005	6,615
Athletics	166,680	42,487	-	(124,193)
Interest on long-term debt	870,290	-	-	(870,290)
Depreciation - unallocated	603,250	-	-	(603,250)
Total governmental activities	\$ 7,621,452	\$ 148,520	\$ 1,083,732	(6,389,200)
General revenues				
Property taxes - operations				2,427,322
Property taxes - debt service				923,218
Grants and contributions not restricted to specific programs				2,669,957
Unrestricted investment earnings				49,131
Total general revenues				6,069,628
Change in net assets				(319,572)
Net assets (deficit), beginning of year				(4,442,159)
Net assets (deficit), end of year				\$ (4,761,731)

The accompanying notes are an integral part of these financial statements.

FUND FINANCIAL STATEMENTS

PELLSTON PUBLIC SCHOOLS

BALANCE SHEET GOVERNMENTAL FUNDS

JUNE 30, 2006

	General	1992 Debt Service Fund	Non- Major Funds	Total
ASSETS				
Cash and cash equivalents	\$ 600,727	\$ 284,981	\$ 224,908	\$ 1,110,616
Investments	1,275,747	-	-	1,275,747
Inventory	-	-	5,212	5,212
Accounts receivable	1,801	-	2,461	4,262
Due from other funds	-	-	120,685	120,685
Due from other governmental units	526,189	-	27,209	553,398
Total assets	\$ 2,404,464	\$ 284,981	\$ 380,475	\$ 3,069,920
LIABILITIES AND FUND BALANCES				
Liabilities				
Accounts payable	\$ 38,835	\$ -	\$ -	\$ 38,835
Salaries payable	393,016	-	8,180	401,196
Accrued expenses	153,231	-	1,392	154,623
Due to other funds	21,245	99,439	1	120,685
Unearned revenue	-	-	25,768	25,768
State aid anticipation note	1,543,678	-	-	1,543,678
Total liabilities	2,150,005	99,439	35,341	2,284,785
Fund balances				
Reserved				
Debt service	-	185,542	305,079	490,621
Inventory	-	-	5,212	5,212
Unreserved				
Designated special revenue funds	-	-	-	-
Undesignated special revenue funds	-	-	34,843	34,843
Undesignated general fund	254,459	-	-	254,459
Total fund balances	254,459	185,542	345,134	785,135
Total liabilities and fund balances	\$ 2,404,464	\$ 284,981	\$ 380,475	\$ 3,069,920

Continued...

PELLSTON PUBLIC SCHOOLS

BALANCE SHEET GOVERNMENTAL FUNDS

JUNE 30, 2006

Reconciliation of fund balance on the balance sheet for governmental funds to net assets of governmental activities on the statement of net assets

Fund balances - total governmental funds	\$ 785,135
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Amounts reported for governmental activities in the statement of net assets are different because

Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds

Add	- capital assets	13,124,316
Deduct	- accumulated depreciation	(7,096,519)

The focus of governmental funds is on short-term financing, some assets will not be available to pay for current-period expenditures. Those assets (such as certain receivables) are offset by unearned revenues in the governmental funds, and thus are not included in fund balance.

Add	- unearned revenues	25,768
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Certain liabilities, such as bonds payable, are not due and payable in the current period and therefore are not reported in the funds

Deduct	- bonds, notes and early retirement payables	(8,896,217)
	- interest accretion on capital appreciation bonds	(2,583,098)
	- accrued interest on bonds payable	(98,788)
	- compensated absences	(22,328)

Net assets (deficit) of governmental activities	<u>\$ (4,761,731)</u>
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Concluded

The accompanying notes are an integral part of these financial statements.

PELLSTON PUBLIC SCHOOLS
STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2006

	<u>General</u>	<u>1992 Debt Service Fund</u>	<u>Non- Major Funds</u>	<u>Total</u>
Revenues				
Local sources				
Property taxes	\$ 2,427,322	\$ 474,086	\$ 449,132	\$ 3,350,540
Charges for services	23,521	-	124,999	148,520
Interest	36,888	7,113	5,130	49,131
Other	37,903	-	-	37,903
State sources	2,977,350	-	9,037	2,986,387
Federal sources	230,278	-	171,968	402,246
Interdistrict sources	328,001	-	-	328,001
Total revenues	6,061,263	481,199	760,266	7,302,728
Expenditures				
Instruction	3,924,933	-	-	3,924,933
Supporting services	1,894,803	-	-	1,894,803
Food services	-	-	256,397	256,397
Athletics	-	-	154,134	154,134
Capital outlay	-	-	13,612	13,612
Debt service				
Principal	62,833	188,356	225,000	476,189
Interest	56,013	272,544	283,576	612,133
Total expenditures	5,938,582	460,900	932,719	7,332,201
Revenues over (under) expenditures	122,681	20,299	(172,453)	(29,473)
Other financing sources (uses)				
Transfers in	8,031	-	185,041	193,072
Transfers out	(185,041)	-	(8,031)	(193,072)
Total other financing sources (uses)	(177,010)	-	177,010	-
Changes in fund balances	(54,329)	20,299	4,557	(29,473)
Fund balances, beginning of year	308,788	165,243	340,577	814,608
Fund balances, end of year	\$ 254,459	\$ 185,542	\$ 345,134	\$ 785,135

Continued...

PELLSTON PUBLIC SCHOOLS
STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS

FOR THE YEAR ENDED JUNE 30, 2006

**Reconciliation of the statement of revenues, expenditures and changes in fund balances
of governmental funds to the statement of activities**

Net change in fund balances - total governmental funds	\$ (29,473)
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Amounts reported for *governmental activities* in the statement of activities is different because

Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.

Add	- capital outlay	68,247
Deduct	- depreciation expense	(614,295)
	- disposal of capital assets	(2,000)

Current revenues in the funds that were recorded as revenues in prior years in the statement of activities.

Deduct	- decrease in unearned revenue related to Durant settlement	(2,112)
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Bond proceeds provide current financial resources to governmental funds in the period issued, but issuing bonds increases long-term liabilities in the statement of net assets. Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets.

Add	- principal payments on long-term liabilities	506,302
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Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the funds.

Add	- decrease in accrued interest payable on bonds	22,856
Deduct	- increase in interest accretion on capital appreciation bonds	(279,997)
Add	- decrease in the accrual for compensated absences	10,900

Change in net assets of governmental activities	\$ (319,572)
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Concluded

The accompanying notes are an integral part of these financial statements.

PELLSTON PUBLIC SCHOOLS

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE - BUDGET AND ACTUAL GENERAL FUND

FOR THE YEAR ENDED JUNE 30, 2006

	Budget			Variance - Positive (Negative) Amended to Actual
	Original	Amended	Actual	
Revenues				
Local sources	\$ 2,529,864	\$ 2,520,102	\$ 2,525,634	\$ 5,532
State sources	2,860,768	2,980,880	2,977,350	(3,530)
Federal sources	235,853	223,331	230,278	6,947
Interdistrict sources	311,350	340,801	328,001	(12,800)
Total revenues	5,937,835	6,065,114	6,061,263	(3,851)
Expenditures				
Education				
Instruction	3,842,606	3,929,279	3,924,933	4,346
Support services	1,834,887	1,889,190	1,894,803	(5,613)
Debt service				
Principal payments	64,406	64,945	62,833	2,112
Interest and paying agent fees	30,000	57,052	56,013	1,039
Total expenditures	5,771,899	5,940,466	5,938,582	1,884
Revenues over (under) expenditures	165,936	124,648	122,681	(1,967)
Other financing sources (uses)				
Transfers in	-	-	8,031	8,031
Transfers out	(162,808)	(177,040)	(185,041)	(8,001)
Total other financing sources (uses)	(162,808)	(177,040)	(177,010)	30
Changes in fund balance	3,128	(52,392)	(54,329)	(1,937)
Fund balance, beginning of year	308,788	308,788	308,788	-
Fund balance, end of year	\$ 311,916	\$ 256,396	\$ 254,459	\$ (1,937)

The accompanying notes are an integral part of these financial statements.

PELLSTON PUBLIC SCHOOLS
STATEMENT OF FIDUCIARY NET ASSETS
AGENCY FUND

JUNE 30, 2006

Assets

Cash and cash equivalents	\$ 32,003
Investments	<u>71,204</u>

Total assets	<u>\$ 103,207</u>
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Liabilities

Scholarships payable	\$ 27,171
Due to others	37,890
Due to student groups	<u>38,146</u>

Total liabilities	<u>\$ 103,207</u>
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The accompanying notes are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting entity

Pellston Public Schools (the “District”) has followed the guidelines of the Governmental Accounting Standards Board’s Statement No. 14 and has determined that no entities should be consolidated into its basic financial statements as component units. Therefore, the reporting entity consists of the primary government financial statements only. The criteria for including a component unit include significant operational or financial relationships with the District.

B. District-wide and fund financial statements

The District-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the non-fiduciary activities of the District. For the most part, the effect of interfund activity has been removed from these statements. *Governmental activities*, which normally are supported by taxes and intergovernmental revenues, are reported separately from *business-type activities*, which rely to a significant extent on fees and charges for support. The District had no *business-type activities* during the 2006 fiscal year.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function or segment. *Program revenues* include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as *general revenues*.

Separate financial statements are provided for governmental funds and fiduciary funds, even though the latter are excluded from the District-wide financial statements. Major individual governmental funds are reported as separate columns in the fund financial statements.

C. Measurement focus, basis of accounting, and financial statement presentation

The District-wide financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. Agency funds also use the accrual basis of accounting, but do not have a measurement focus.

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

Governmental fund financial statements are reported using the *current financial resources measurement* focus and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the District considers revenues to be available if they are collected within 60 days of the end of the current fiscal period or within one year for reimbursement type grants. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the government.

The District reports the following major governmental funds:

The *General Fund* is the government's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

The *1992 Debt Service Fund* accounts for assets accumulated to repay the 1992 General Obligation Capital Appreciation Bonds.

Additionally, the District reports the following fund types:

The *Special Revenue Funds* account for the various food service and athletic programs sponsored by the District.

The *Debt Service Funds* account for the principal and interest payments on the bonds used to finance various construction projects in the District.

The *Capital Project Funds* account for various construction projects within the District.

The *Agency Fund* accounts for assets held for other groups and organizations and is custodial in nature.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in the District-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board.

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

When both restricted and unrestricted resources are available for use, it is the District's policy to use restricted resources first, then unrestricted resources as they are needed.

Amounts reported as *program revenues* include 1) charges to customers or applicants for goods, services, or privileges provided and 2) operating grants and contributions. Internally dedicated resources are reported as *general revenues* rather than as program revenues. Likewise, general revenues include all taxes.

The effect of interfund activity has been eliminated from the District-wide financial statements.

D. Assets, liabilities and equity

1. *Deposits*

The District's cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition.

2. *Receivables and payables*

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). There were no interfund advances outstanding at June 30, 2006.

3. *Inventory*

Inventory is valued at the lower of cost (first-in, first-out) or market. Inventory consists of expendable supplies held for consumption. The cost is recorded as an expenditure when consumed rather than when purchased. Reported inventories are equally offset by a fund balance reserve which indicates that they do not constitute "available spendable resources" even though they are a component of net current assets.

4. *Capital assets*

Capital assets, which include property and equipment, are reported in the District-wide financial statements. Capital assets are defined by the District as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair value at the date of donation.

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Capital assets of the District are depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings and improvements	20-50
Land improvements	20
Equipment	5-20
Vehicles	7-10

5. *Compensated absences*

District policy permits certain employees to accumulate earned but unused sick pay benefits which are paid when the employee separates from service with the District. A liability is recorded in the statement of net assets for such amounts. No liability is recorded for accumulated vacation since hours earned do not vest.

6. *Long-term obligations*

In the District-wide financial statements, long-term obligations are reported as liabilities in the statement of net assets. Where applicable, bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

7. *Fund equity*

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

II. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgetary information

The General and Special Revenue Funds are under formal budgetary control. Budgets shown in the financial statements are adopted on a basis consistent with accounting principles generally accepted in the United States of America (GAAP), and are not significantly different from the modified accrual basis used to reflect actual results, and consist only of those amounts contained in the formal budget as originally adopted or as amended by the Board of Education. The budgets for the General and Special Revenue Funds are adopted on a functional basis.

B. Excess of expenditures over appropriations

Expenditures in excess of budgeted amounts at the legal level of control are disclosed in the Statement of Revenues, Expenditures and Changes in Fund Balance – Budget and Actual for the General Fund.

III. DETAILED NOTES ON ALL FUNDS

A. Deposits and investments

A reconciliation of cash and cash equivalents as shown on the Statement of Net Assets and Statement of Fiduciary Net Assets is as follows:

Statement of Net Assets	
Cash and cash equivalents	\$ 1,110,616
Investments	<u>1,275,747</u>
Total Statement of Net Assets	<u>\$ 2,386,363</u>
Statement of Fiduciary Net Assets	
Agency Fund	
Cash and cash equivalents	\$ 32,003
Investments	<u>71,204</u>
Total deposits and investments	<u>\$ 2,489,570</u>

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

A reconciliation of cash and investments as shown in the financial statements to the District's deposits and investments is as follows:

Bank deposits	\$ 1,141,819
Investments	1,346,951
Cash on hand	<u>800</u>
Total deposits and investments	<u>\$ 2,489,570</u>

The District believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all bank deposits. As a result, the District evaluates each financial institution with which it deposits funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

Michigan law authorizes the District to deposit and invest in:

- (a) Bonds, bills, or notes of the United States; obligations, the principal and interest of which are fully guaranteed by the United States; or obligations of the State. In a primary or fourth class school district, the bonds, bills, or notes shall be payable at the option of the holder upon not more than 90 days notice or, if not so payable, shall have maturity dates not more than 5 years after the purchase dates.
- (b) Certificates of deposit insured by a state or national bank, savings accounts of a state or federal savings and loan association, or certificates of deposit or share certificates of a state or federal credit union organized and authorized to operate in this state.
- (c) Commercial paper rated prime at the time of purchase and maturing not more than 270 days after the date of purchase.
- (d) Securities issued or guaranteed by agencies or instrumentalities of the United States government or federal agency obligation repurchase agreements, and bankers' acceptance issued by a bank that is a member of the federal deposit insurance corporation.
- (e) Mutual funds composed entirely of investment vehicles that are legal for direct investment by a school district.
- (f) Investment pools, as authorized by the surplus funds investment pool act, composed entirely of instruments that are legal for direct investment by a school district.

The District's investment policy allows for all of these types of investments.

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

The District chooses to disclose its investments by specifically identifying each. As of year end, the District had the following deposits and investments:

<u>Deposit/Investment</u>	<u>Maturity</u>	<u>Fair Value</u>	<u>Rating</u>
Bank deposits including certificates of deposit	n/a	\$ 1,162,300	n/a
Michigan Liquid Asset Fund	n/a	1,326,470	S&P – AAAM
Cash on hand	n/a	<u>800</u>	n/a
		<u>\$ 2,489,570</u>	

Investment and deposit risk

Interest Rate Risk. State law limits the allowable investments and the maturities of some of the allowable investments as identified above. The District's investment policy does not have specific limits in excess of state law on investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk. State law limits investments to specific government securities, certificates of deposits and bank accounts with qualified financial institutions, commercial paper with specific maximum maturities and ratings when purchased, bankers acceptances of specific financial institutions, qualified mutual funds and qualified external investment pools as identified in the list of authorized investments above. The District's investment policy does not have specific limits in excess of state law on investment credit risk. The ratings for each investment are identified above for investments held at year end.

Custodial Credit Risk – Deposits. Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned. State law does not require and the District does not have a policy for deposit custodial credit risk. As of year end, \$1,182,382 of the District's bank balance of \$1,333,105 was exposed to custodial credit risk because it was uninsured and uncollateralized.

Custodial Credit Risk – Investments. For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the District will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. State law does not require and the District does not have a policy for investment custodial credit risk. On the investments listed above, there is no custodial credit risk, as these investments are uncategorized as to credit risk.

Concentration of Credit Risk. State law limits allowable investments but does not limit concentration of credit risk as identified in the list of authorized investments above. The District's investment policy does not have specific limits in excess of state law on concentration of credit risk. All investments held at year end are reported above.

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

B. Receivables

Receivables in the governmental activities totaling \$557,660 are made up of \$553,398 in due from other governmental units, and \$4,262 from accounts receivable in the hot lunch and general fund. All receivables, except for the amount due from the Durant bonds of \$25,768, are expected to be collected within the next fiscal year.

C. Capital assets

Capital assets activity was as follows for the year ended June 30, 2006:

	Balance July 1, 2005	Additions	Disposals	Balance June 30, 2006
Capital assets not being depreciated				
Land	\$ 35,000	\$ -	\$ -	\$ 35,000
Capital assets being depreciated				
Buildings and improvements	11,379,709	27,943	-	11,407,652
Land improvements	75,000	-	-	75,000
Equipment	965,631	40,304	-	1,005,935
Vehicles	641,352	-	40,623	600,729
Subtotal	<u>13,061,692</u>	<u>68,247</u>	<u>40,623</u>	<u>13,089,316</u>
Accumulated depreciation				
Buildings and improvements	(5,492,516)	(509,019)	-	(6,001,535)
Land improvements	(32,750)	(3,750)	-	(36,500)
Equipment	(602,844)	(59,900)	-	(662,744)
Vehicles	(392,737)	(41,626)	38,623	(395,740)
Total accumulated depreciation	<u>(6,520,847)</u>	<u>(614,295)</u>	<u>38,623</u>	<u>(7,096,519)</u>
Total capital assets being depreciated, net	<u>6,540,845</u>	<u>(546,048)</u>	<u>(2,000)</u>	<u>5,992,797</u>
Capital assets, net	<u>\$6,575,845</u>	<u>\$ (546,048)</u>	<u>\$ (2,000)</u>	<u>\$6,027,797</u>

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

Depreciation expense was charged to functions/programs of the District as follows:

Governmental activities

Athletics	\$ 11,045
Unallocated	<u>603,250</u>
Total depreciation expense – governmental activities	<u>\$ 614,295</u>

D. Accounts payable and accrued expenses

Payables are comprised of the following:

Accounts payable	\$ 38,835
Salaries payable	401,196
Accrued expenses	<u>253,411</u>
Total accounts payable and accrued expenses	<u>\$ 693,442</u>

E. Interfund receivables, payables and transfers

The following balances represent individual fund interfund receivables and payables at June 30, 2006:

	<u>Interfund Receivables</u>	<u>Interfund Payables</u>
General Fund	\$ -	\$ 21,245
1992 Debt Service Fund	-	99,439
Nonmajor Funds	<u>120,685</u>	<u>1</u>
Total	<u>\$120,685</u>	<u>\$ 120,685</u>

The District reports interfund balances between certain funds. The sum of all balances presented in the tables above agrees with the sum of interfund balances presented in the balance sheet for governmental funds. These interfund balances resulted primarily from the time lag between the dates that (1) interfund goods and services are provided or reimbursable expenditures occur, (2) transactions are recorded in the accounting system and (3) payments between funds are made.

For the year ended June 30, 2006, interfund transfers consisted of subsidy transfers from the General Fund to the nonmajor Athletic Fund and Energy Bonds Debt Service Fund of \$115,383 and \$69,658, respectively. The Food Service Fund and Capital Projects Fund made transfers to the General Fund for \$8,000 and \$31 respectively.

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

F. Long-term debt

A summary of long-term debt and transactions related thereto is as follows for the year ended June 30, 2006:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>(Reductions)</u>	<u>Ending Balance</u>	<u>Amount Due Within One Year</u>
2002 School Building and Site Construction Bonds, due through May 2016 in semi-annual installments of interest and annual principal payments varying from \$165,000 - \$240,000 bearing interest rates ranging from 4.25% to 4.375%.	\$ 2,285,000	\$ -	\$ (145,000)	\$ 2,140,000	\$ 165,000
1998 General Obligation Refunding Bonds, due through May 2012 in semi-annual installments of interest and annual principal payments varying from \$35,000 - \$800,000 with interest rates ranging from 4.40% to 4.75%.	3,475,000	-	(35,000)	3,440,000	35,000
1993 General Obligation Refunding Bonds, due from May 2013 through May 2022 in annual installments of interest and annual principal payments varying from \$189,900 - \$284,638 with interest rates ranging from 5.70% to 5.90%.	2,437,230	-	-	2,437,230	-

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

	<u>Beginning Balance</u>	<u>Additions</u>	<u>(Reductions)</u>	<u>Ending Balance</u>	<u>Amount Due Within One Year</u>
1992 General Obligation Capital Appreciation Bonds, due through May 2007 in semi-annual installments of interest and an annual principal payment of \$186,444 with an interest rate of 6.80%.	\$ 374,800	\$ -	\$ (188,356)	\$ 186,444	\$ 186,444
2004 Energy Conservation Improvement Bonds due through May 2015 in semi-annual installments of interest and principal payments varying from \$50,000 - \$70,000 with an interest rate of 4.21%	575,000	-	(45,000)	530,000	50,000
Durant Settlement Bonds, due through May 2013 in annual installments of principal payments varying from \$2,212 to \$10,310, including interest charged at 4.76%.	27,880	-	(2,112)	25,768	2,212
Various bus notes payable, due from July 15, 2006 through September 22, 2009 in annual installments of interest and principal installments aggregating from \$10,822 through \$43,388 with interest rates ranging from 2.87% to 3.88%.	171,609	-	(62,834)	108,775	43,388

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

	<u>Beginning Balance</u>	<u>Additions</u>	<u>(Reductions)</u>	<u>Ending Balance</u>	<u>Amount Due Within One Year</u>
Early retirement payable.	\$ 56,000	\$ -	\$ (28,000)	\$ 28,000	\$ 28,000
Interest accretion on the 1992 capital appreciation bonds.	2,303,101	279,997	-	2,583,098	-
Compensated absences.	33,228	-	(10,900)	22,328	-
Total long-term debt	<u>\$ 11,738,848</u>	<u>\$ 279,997</u>	<u>\$ (517,202)</u>	<u>\$11,501,643</u>	<u>\$ 510,045</u>

The Durant School Improvement Bonds are serviced from funds made available to Michigan School Districts by an annual appropriation by the Michigan State Legislature. If the Legislature does not appropriate the funding required, the District is not liable to pay the debt service.

Debt service requirements

Annual debt service requirements to maturity for the above obligations except for the compensated absences are as follows:

<u>Years Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2007	\$ 510,045	\$ 579,405	\$ 1,089,450
2008	829,832	263,625	1,093,457
2009	897,362	231,073	1,128,435
2010	948,366	188,499	1,136,865
2011	1,017,665	146,293	1,163,958
2012-2016	3,356,762	2,778,638	6,135,400
2017-2021	1,146,285	3,878,555	5,024,840
2022	189,900	810,100	1,000,000
Total	<u>\$ 8,896,217</u>	<u>\$ 8,876,188</u>	<u>\$17,772,405</u>

During fiscal 2006 the District repaid the 2004 state aid anticipation note of \$1,400,000, which had a balance of \$ 191,083 on June 30, 2005. On August 19, 2005, the District borrowed \$1,500,000 on a 2005 state aid anticipation note. At June 30, 2006, the balance outstanding on this note was \$1,543,678, including accrued interest.

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

IV. OTHER INFORMATION

A. Risk management

The District is exposed to various risks of loss related to property loss, torts, errors and omissions, employee injuries (workers' compensation) as well as medical benefits provided to employees. The District has purchased commercial insurance for general liability, property and casualty and health claims and participates in the MASB/SET-SEG (risk pool) for claims relating to employee injuries/workers' compensation. Settled claims relating to the commercial insurance have not exceeded the amount of insurance coverage in any of the past three fiscal years.

The shared-risk pool program in which the District participates operates as a common risk-sharing management program for school districts in Michigan; member premiums are used to purchase commercial excess insurance coverage and to pay member claims in excess of deductible amounts.

B. Property taxes

Property taxes are assessed as of December 31, and attach as an enforceable lien on property as of July 1 of the following year. Taxes are levied on July 1 by the municipalities within the District, and are due on February 14. Delinquent real taxes are advanced to the District by the revolving tax fund of the applicable county.

C. Defined benefit pension plan

Plan Description

The District contributes to the Michigan Public School Employees Retirement System (MPERS), a cost-sharing multiple-employer defined benefit pension plan administered by the State of Michigan Department of Management and Budget, Office of Retirement Systems. MPERS provides retirement, survivor and disability benefits, and death benefits to plan members and beneficiaries. Benefit provisions are established and must be amended by state statute.

The Office of Retirement Systems issues a publicly available financial report that includes financial statements and required supplementary information for MPERS. That report may be obtained by writing to Michigan Public School Employees Retirement System, 7150 Harris Drive, P.O. Box 30171, Lansing, Michigan, 48909 or by calling 1-800-381-5111.

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

Funding Policy

Member Investment Plan (MIP) members enrolled in MIP prior to January 1, 1990 contribute at a permanently fixed rate of 3.9% of gross wages. Members first hired January 1, 1990 or later contribute at the following graduated permanently fixed contribution rate: 3% of the first \$5,000; 3.6% of \$5,001 through \$15,000; 4.3% of all wages over \$15,000. Basic plan members make no contributions. The District is required to contribute the full actuarial funding contribution amount to fund pension benefits, plus an additional amount to fund retiree health care benefits on a cash disbursement basis.

The current rate is 16.34% of annual covered payroll. The contribution requirements of plan members and the District are established by Michigan State statute and may be amended only by action of the State Legislature. The District's contributions to MPSERS for the years ended June 30, 2006, 2005 and 2004 were approximately \$550,000, \$496,000, and \$429,000, respectively, equal to the required contributions for each year.

Other Post-employment Benefits

Retirees have the option of health coverage which is funded on a cash disbursement basis by the District. The State of Michigan has contracted to provide the comprehensive group medical, hearing, dental and vision coverage for retirees and beneficiaries. All health care benefits are on a self-funded basis. A significant portion of the premium is paid by MPSERS with the balance deducted from the monthly pension.

Pension recipients are eligible for fully paid master health plan coverage and 90% paid dental plan, vision plan and hearing plan coverage with the following exceptions:

1. Retirees not yet eligible for Medicare coverage pay an amount equal to the Medicare Part B premiums.
2. Retirees with less than 30 years of service, who terminate employment after October 31, 1980 with the vested deferred benefits, are eligible for partially employer paid health benefit coverage (no payment if less than 21 years of service).

PELLSTON PUBLIC SCHOOLS
NOTES TO THE FINANCIAL STATEMENTS

D. Commitments and contingencies

Under the terms of various federal and state grants and regulatory requirements, periodic audits are required and certain cost may be questioned as not being appropriate expenditures under the terms of the grants and requirements. Such audits could lead to reimbursement of the grantor or regulatory agencies. However, management does not believe such disallowances, if any, would be material to the financial position of the district.

As is the case with other entities, the District faces exposure from potential claims and legal proceedings involving environmental matters. No such claims or proceedings have been asserted as of June 30, 2006.

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SUPPLEMENTARY INFORMATION

PELLSTON PUBLIC SCHOOLS
COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS

JUNE 30, 2006

	Special Revenue Funds		Debt Service Funds		
	Food Service	Athletics	1998 Debt	2002 Debt	Energy Bonds
ASSETS					
Cash and cash equivalents	\$ 7,085	\$ 12,183	\$ 43,013	\$ 162,627	\$ -
Account receivable	2,461	-	-	-	-
Inventory	5,212	-	-	-	-
Due from other funds	20,499	746	95,935	3,505	-
Due from other governmental units	1,441	-	-	-	-
Total assets	\$ 36,698	\$ 12,929	\$ 138,948	\$ 166,132	\$ -
LIABILITIES AND FUND BALANCES					
Liabilities					
Salaries payable	\$ 6,396	\$ 1,784	\$ -	\$ -	\$ -
Accrued expenses	1,255	137	-	-	-
Due to other funds	-	-	-	1	-
Deferred revenue	-	-	-	-	-
Total liabilities	7,651	1,921	-	1	-
Fund balances					
Reserved for debt service	-	-	138,948	166,131	-
Reserved for inventory	5,212	-	-	-	-
Unreserved, undesignated	23,835	11,008	-	-	-
Total fund balances	29,047	11,008	138,948	166,131	-
Total liabilities and fund balances	\$ 36,698	\$ 12,929	\$ 138,948	\$ 166,132	\$ -

	Capital Project Fund	
Durant Settlement	Building Construction	Total
\$ -	\$ -	\$ 224,908
-	-	2,461
-	-	5,212
-	-	120,685
25,768	-	27,209
\$ 25,768	\$ -	\$ 380,475

\$ -	\$ -	\$ 8,180
-	-	1,392
-	-	1
25,768	-	25,768
25,768	-	35,341
-	-	305,079
-	-	5,212
-	-	34,843
-	-	345,134
\$ 25,768	\$ -	\$ 380,475

PELLSTON PUBLIC SCHOOLS

COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE NONMAJOR GOVERNMENTAL FUNDS

FOR THE YEAR ENDED JUNE 30, 2006

	Special Revenue Funds		Debt Service Funds		
	Food Service	Athletics	1998 Debt	2002 Debt	Energy Bonds
Revenues					
Local sources					
Property taxes	\$ -	\$ -	\$ 174,663	\$ 274,469	\$ -
Charges for services	82,512	42,487	-	-	-
Interest	314	260	1,386	2,948	-
State sources	9,037	-	-	-	-
Federal sources	171,968	-	-	-	-
Total revenues	263,831	42,747	176,049	277,417	-
Expenditures					
Food services					
Salaries	107,893	-	-	-	-
Employee benefits	34,705	-	-	-	-
Purchased services	4,212	-	-	-	-
Supplies, material and other expenses	109,587	-	-	-	-
Total food service	256,397				
Athletics					
Salaries	-	84,079	-	-	-
Employee benefits	-	15,551	-	-	-
Purchased services	-	22,913	-	-	-
Supplies, material and other expenses	-	31,591	-	-	-
Total athletics	-	154,134	-	-	-
Capital outlay	535	1,501	-	-	-
Debt service					
Principal	-	-	35,000	145,000	45,000
Interest and fees	-	-	161,005	97,913	24,658
Total expenditures	256,932	155,635	196,005	242,913	69,658
Revenues over (under) expenditures	6,899	(112,888)	(19,956)	34,504	(69,658)
Other financing sources (uses)					
Transfers in	-	115,383	-	-	69,658
Transfers out	(8,000)	-	-	-	-
Total other financing sources (uses)	(8,000)	115,383	-	-	69,658
Changes in fund balances	(1,101)	2,495	(19,956)	34,504	-
Fund balances, beginning of year	30,148	8,513	158,904	131,627	-
Fund balances, end of year	\$ 29,047	\$ 11,008	\$ 138,948	\$ 166,131	\$ -

	Capital	
	Project Fund	
Durant	Building	
Settlement	Construction	Total
\$ -	\$ -	\$ 449,132
-	-	124,999
-	222	5,130
-	-	9,037
-	-	171,968
-	222	760,266
-	-	107,893
-	-	34,705
-	-	4,212
-	-	109,587
		256,397
-	-	84,079
-	-	15,551
-	-	22,913
-	-	31,591
-	-	154,134
-	11,576	13,612
-	-	225,000
-	-	283,576
-	11,576	932,719
-	(11,354)	(172,453)
-	-	185,041
-	(31)	(8,031)
-	(31)	177,010
-	(11,385)	4,557
-	11,385	340,577
\$ -	\$ -	\$ 345,134

PELLSTON PUBLIC SCHOOLS

**BALANCE SHEET
GENERAL FUND**

**JUNE 30, 2006
(WITH COMPARATIVE TOTALS FOR JUNE 30, 2005)**

	2006	2005
ASSETS		
Cash and cash equivalents	\$ 600,727	\$ 451,930
Investments	1,275,747	-
Taxes receivable	-	89,765
Accounts receivable	1,801	-
Due from other governmental units	526,189	595,158
Total assets	\$ 2,404,464	\$ 1,136,853
LIABILITIES AND FUND BALANCE		
Liabilities		
Accounts payable	\$ 38,835	\$ 63,419
Salaries payable	393,016	382,076
Accrued expenses	153,231	158,103
Due to other funds	21,245	21,467
Due to other governmental units	-	11,917
State aid anticipation note	1,543,678	191,083
Total liabilities	2,150,005	828,065
Fund balance		
Unreserved		
Undesignated	254,459	308,788
Total liabilities and fund balance	\$ 2,404,464	\$ 1,136,853

PELLSTON PUBLIC SCHOOLS

SCHEDULE OF REVENUES AND OTHER FINANCING SOURCES GENERAL FUND

FOR THE YEAR ENDED JUNE 30, 2006
(WITH COMPARATIVE AMOUNTS FOR THE YEAR ENDED, JUNE 30, 2005)

	2006	2005
Revenues		
Local sources		
Property taxes	\$ 2,427,322	\$ 2,214,694
Charge for services	23,521	23,084
Interest	36,888	11,381
Other local revenue	37,903	22,233
Total local sources	2,525,634	2,271,392
State sources		
State aid	2,965,638	3,007,136
Other state revenue	11,712	14,497
Total state sources	2,977,350	3,021,633
Federal sources		
Title I	150,952	158,093
Title II	53,768	56,920
Title V	3,200	4,704
Title IX	20,957	17,225
Other	1,401	1,778
Total federal sources	230,278	238,720
Interdistrict sources	328,001	332,183
Other financing sources		
Transfers In	8,031	-
Loan proceeds	-	54,110
Total other financing sources	8,031	54,110
Total revenues and other financing sources	\$ 6,069,294	\$ 5,918,038

PELLSTON PUBLIC SCHOOLS

SCHEDULE OF EXPENDITURES AND OTHER FINANCING USES GENERAL FUND

FOR THE YEAR ENDED JUNE 30, 2006
(WITH COMPARATIVE AMOUNTS FOR THE YEAR ENDED, JUNE 30, 2005)

	2006	2005
Expenditures		
Instruction		
Basic programs		
Elementary		
Salaries	\$ 964,019	\$ 930,695
Employee benefits	437,037	419,034
Purchased services	4,352	2,305
Supplies, materials and other expense	18,468	17,378
Total elementary	1,423,876	1,369,412
Middle school		
Salaries	496,210	365,418
Employee benefits	226,416	170,330
Purchased services	753	488
Supplies, materials and other expense	13,478	9,861
Total middle school	736,857	546,097
High school		
Salaries	556,515	661,194
Employee benefits	284,546	299,077
Purchased services	15,035	66,240
Supplies, materials and other expense	34,189	24,270
Total high school	890,285	1,050,781
Total basic programs	3,051,018	2,966,290
Added needs		
Special education		
Salaries	346,707	339,671
Employee benefits	184,258	171,883
Purchased services	-	162
Supplies, materials and other expense	4,031	2,285
Total special education	534,996	514,001
Compensatory education		
Salaries	117,010	152,675
Employee benefits	54,933	68,079
Purchased services	65,134	973
Supplies, materials and other expense	3,065	3,412
Total compensatory education	240,142	225,139

Continued...

PELLSTON PUBLIC SCHOOLS

SCHEDULE OF EXPENDITURES AND OTHER FINANCING USES GENERAL FUND

FOR THE YEAR ENDED JUNE 30, 2006
(WITH COMPARATIVE AMOUNTS FOR THE YEAR ENDED, JUNE 30, 2005)

	2006	2005
Vocational education		
Salaries	\$ 49,186	\$ 44,863
Employee benefits	26,841	24,357
Purchased services	162	-
Supplies, materials and other expense	2,561	160
Capital outlay	20,027	20,570
Total vocational education	98,777	89,950
Total added needs	873,915	829,090
Total instruction	3,924,933	3,795,380
Supporting services		
Pupil services		
Guidance services		
Salaries	112,196	112,005
Employee benefits	51,519	47,355
Purchased services	724	605
Supplies, materials and other expense	-	-
Total pupil services	164,439	159,965
Instructional staff services		
Improvement of instruction		
Salaries	-	6,300
Employee benefits	12,699	13,419
Purchased services	7,926	14,508
Total improvement of instruction	20,625	34,227
Library		
Salaries	19,973	15,964
Employee benefits	9,713	7,741
Purchased services	-	199
Supplies, materials and other expense	752	1,490
Total library	30,438	25,394
Supervision of instructional staff		
Salaries	23,573	41,948
Employee benefits	5,859	11,037
Total supervision of instructional staff	29,432	52,985
Total instructional staff services	80,495	112,606

Continued...

PELLSTON PUBLIC SCHOOLS

SCHEDULE OF EXPENDITURES AND OTHER FINANCING USES GENERAL FUND

FOR THE YEAR ENDED JUNE 30, 2006
(WITH COMPARATIVE AMOUNTS FOR THE YEAR ENDED, JUNE 30, 2005)

	2006	2005
Board of education		
Salaries	\$ 6,962	\$ 8,339
Benefits	94	154
Purchased services	17,148	15,975
Supplies, materials and other expense	10,984	9,491
Total board of education	35,188	33,959
Executive administration		
Salaries	124,094	120,544
Employee benefits	51,331	48,883
Purchased services	20,293	15,634
Supplies, materials and other expense	7,556	8,494
Total executive administration	203,274	193,555
Total general administration	238,462	227,514
School administration		
Office of the principal		
Salaries	304,844	303,619
Employee benefits	126,365	123,013
Purchased services	32,558	31,304
Supplies, materials and other expense	4,660	7,271
Total school administration	468,427	465,207
Business services		
Fiscal services		
Purchased services	86,950	104,276
Supplies, materials and other expense	626	1,243
Capital outlay	5,130	-
Total business services	92,706	105,519

Continued...

PELLSTON PUBLIC SCHOOLS

**SCHEDULE OF EXPENDITURES AND OTHER FINANCING USES
GENERAL FUND**

**FOR THE YEAR ENDED JUNE 30, 2006
(WITH COMPARATIVE AMOUNTS FOR THE YEAR ENDED, JUNE 30, 2005)**

	<u>2006</u>	<u>2005</u>
Transportation		
Salaries	\$ 157,366	\$ 150,443
Employee benefits	49,383	42,508
Purchased services	14,997	21,490
Supplies, materials and other expense	61,108	58,546
Capital outlay	-	56,110
Total transportation	<u>282,854</u>	<u>329,097</u>
Operation and maintenance		
Salaries	121,351	118,167
Employee benefits	60,369	65,074
Purchased services	145,552	194,796
Supplies, materials and other expense	209,134	193,496
Capital outlay	31,014	-
Total operation and maintenance	<u>567,420</u>	<u>571,533</u>
Total support services	<u>1,894,803</u>	<u>1,971,441</u>
Total operating expenditures	<u>5,819,736</u>	<u>5,766,821</u>
Debt service		
Principal	62,833	61,902
Interest and fiscal charges	56,013	20,562
Total debt service	<u>118,846</u>	<u>82,464</u>
Total expenditures	5,938,582	5,849,285
Other financing uses		
Transfers out	<u>185,041</u>	<u>113,709</u>
Total expenditures and other financing uses	<u><u>\$ 6,123,623</u></u>	<u><u>\$ 5,962,994</u></u>

Concluded

PELLSTON PUBLIC SCHOOLS

STATEMENT OF CHANGES IN ASSETS AND LIABILITIES AGENCY FUND

FOR THE YEAR ENDED JUNE 30, 2006

	Balances July 1, 2005	Receipts	Disbursements	Balances June 30, 2006
ASSETS				
Cash and cash equivalents	\$ 69,814	\$ 166,803	\$ 204,614	\$ 32,003
Investments	20,022	51,182	-	71,204
Total assets	\$ 89,836	\$ 217,985	\$ 204,614	\$ 103,207
LIABILITIES				
Scholarships payable	\$ 26,679	\$ 7,028	\$ 6,536	\$ 27,171
Due to others	27,003	89,776	78,889	37,890
Due to student groups	36,154	70,464	68,472	38,146
Total liabilities	\$ 89,836	167,268	\$ 153,897	\$ 103,207
The balances consist of the following:				
Cadwell Scholarship	\$ 20,082	\$ 1,524	\$ 1,000	\$ 20,606
Hayes Scholarship	1,441	3,200	3,200	1,441
Johnson Scholarship	3,000	-	500	2,500
Mini grants	836	-	836	-
PEA Scholarship	76	-	-	76
Sports Boost Scholarship	-	2,300	1,000	1,300
Walsh Scholarship	1,244	4	-	1,248
Total scholarships payable	\$ 26,679	\$ 7,028	\$ 6,536	\$ 27,171
Academic boosters	\$ 22	\$ -	\$ 22	\$ -
Athletic - general	759	1,003	1,165	597
Band boosters	470	15,860	13,983	2,347
Beverage concessions	9,602	9,297	8,663	10,236
Casual wear	933	157	232	858
Christmas/needy	563	2,979	3,230	312
Elementary social fund	125	420	479	66
Elementary teacher's pop	910	2,955	3,324	541
Field trip transportation	325	-	-	325
Interest	3,198	3,724	5,573	1,349
McClutchey field improvement	984	16,331	5,315	12,000
Office concessions	102	1,057	153	1,006
Principal - elementary	263	1,962	1,051	1,174
Principal - high school	1,425	2,311	1,708	2,028
Principal - middle school	53	1,200	971	282
Reading is fundamental/book fair	2,137	7,027	7,676	1,488
Sports boosters	2,820	21,557	23,610	767
Safety Sam	1,604	306	306	1,604
Spitzi counseling	16	-	16	-
Weitzel - track	355	826	826	355
Woodshop	337	804	586	555
Total due to others	\$ 27,003	\$ 89,776	\$ 78,889	\$ 37,890

PELLSTON PUBLIC SCHOOLS

STATEMENT OF CHANGES IN ASSETS AND LIABILITIES AGENCY FUND

FOR THE YEAR ENDED JUNE 30, 2006

	Balances July 1, 2005	Receipts	Disbursements	Balances June 30, 2006
Annual (yearbook)	\$ 3,197	\$ 10,191	\$ 12,278	\$ 1,110
Art department	1,537	250	565	1,222
Boys baseball	580	2,797	1,622	1,755
Cheerleaders - high school	107	-	107	-
Cheerleaders - middle school	720	1,378	1,471	627
Elementary school cash	1,362	664	642	1,384
Fourth and fifth girls club	184	-	184	-
Girls varsity basketball	377	2,334	2,370	341
Girls varsity softball	168	1,156	1,273	51
High school drama club	1,176	1,710	1,756	1,130
Middle school drama	100	-	-	100
Middle school girls basketball	155	105	102	158
Multicultural - sixth	378	-	-	378
National Honor Society	364	700	637	427
Renaissance	254	1,000	87	1,167
SADD	581	431	388	624
Ski club	281	1,787	1,920	148
Spanish club	230	-	-	230
STAND	678	-	600	78
START	1,002	1,187	1,501	688
Student council - high school	1,666	2,208	2,685	1,189
Student council - middle school	706	2,258	3,059	(95)
Student flow	181	4,457	4,354	284
Varsity boys basketball	801	471	86	1,186
Varsity football	1,437	3,139	2,529	2,047
Volleyball	475	8,092	6,156	2,411
Youth enrichment - ski club	144	508	199	453
Kindergarten	468	2,293	1,968	793
First grade	467	1,416	945	938
Second grade	548	503	293	758
Third grade	716	936	645	1,007
Fourth grade	353	1,195	1,025	523
Fifth grade	892	2,944	3,026	810
Class of 2012	-	6,728	4,241	2,487
Class of 2011	1,138	266	94	1,310
Class of 2010	1,111	152	80	1,183
Class of 2009	2,413	117	111	2,419
Class of 2008	3,563	1,737	1,535	3,765
Class of 2007	3,536	2,554	5,130	960
Class of 2006	1,724	916	2,150	490
Class of 2005	255	-	217	38
Class of 2004	129	-	-	129
Elementary building drama	-	1,406	441	965
Math department MS/HS	-	478	-	478
Total due to student groups	\$ 36,154	\$ 70,464	\$ 68,472	\$ 38,146

PELLSTON PUBLIC SCHOOLS

SCHEDULE OF INDEBTEDNESS

JUNE 30, 2006

	<u>Date of Note</u>	<u>Amount of Note</u>	<u>Interest Rate</u>	<u>Date of Maturity</u>	<u>Total Outstanding at June 30, 2006</u>	<u>Total Interest Payable</u>
2002 School Building and Site Construction Bonds	2/1/2002	\$ 2,600,000	4.250%	11/1/2006	\$ -	\$ 45,625
			4.250%	5/1/2007	165,000	45,625
			4.250%	11/1/2007	-	42,119
			4.250%	5/1/2008	180,000	42,119
			4.250%	11/1/2008	-	38,294
			4.250%	5/1/2009	190,000	38,294
			4.250%	11/1/2009	-	34,256
			4.250%	5/1/2010	200,000	34,256
			4.250%	11/1/2010	-	30,006
			4.250%	5/1/2011	215,000	30,006
			4.250%	11/1/2011	-	25,438
			4.250%	5/1/2012	235,000	25,438
			4.250%	11/1/2012	-	20,444
			4.250%	5/1/2013	235,000	20,444
			4.250%	11/1/2013	-	15,450
			4.250%	5/1/2014	240,000	15,450
			4.250%	11/1/2014	-	10,350
			4.250%	5/1/2015	240,000	10,350
			4.250%	11/1/2015	-	5,250
			4.375%	5/1/2016	240,000	5,250
				<u>\$ 2,140,000</u>	<u>\$ 534,464</u>	

Note: Bonds of this issue maturing in the fiscal years 2006 through 2011, inclusive, shall not be subject to redemption prior to maturity. Bonds or portions of Bonds in multiples of \$5,000 of this issue maturing in the year 2012 and thereafter, shall be subject to redemption prior to maturity, at the option of the Issuer, in such order as the Issuer may determine and by lot within any maturity, on any interest payment date on or after May 1, 2011, at par and accrued interest to the date fixed for redemption.

PELLSTON PUBLIC SCHOOLS

SCHEDULE OF INDEBTEDNESS

JUNE 30, 2006

	Date of Note	Amount of Note	Interest Rate	Date of Maturity	Total Outstanding at June 30, 2006	Total Interest Payable
1998 General Obligation Refunding Bonds	6/30/1998	\$ 3,720,000	4.400%	5/1/2007	\$ 35,000	\$ 157,932
			4.450%	5/1/2008	565,000	156,392
			4.500%	5/1/2009	620,000	131,250
			4.550%	5/1/2010	680,000	103,350
			4.650%	5/1/2011	740,000	72,410
			4.750%	5/1/2012	800,000	38,000
					\$ 3,440,000	\$ 659,334

Note: The Bonds or portions of the Bonds in multiples of \$5,000 maturing on or after May 1, 2009 are subject to redemption at the option of the District in such order as the District may determine by lot within any maturity, on any interest payment date occurring on or after May 1, 2008, at par plus accrued interest to the date fixed for redemption.

PELLSTON PUBLIC SCHOOLS

SCHEDULE OF INDEBTEDNESS

JUNE 30, 2006

	<u>Date of Note</u>	<u>Amount of Note</u>	<u>Interest Rate</u>	<u>Date of Maturity</u>	<u>Total Outstanding at June 30, 2006</u>	<u>Total Interest Payable</u>
1993 General Obligation Refunding Bonds	10/6/93	\$ 2,437,230	5.70%	5/1/2013	\$ 284,638	\$ 570,362
			5.70%	5/1/2014	281,674	613,326
			5.85%	5/1/2015	269,186	664,493
			5.85%	5/1/2016	265,548	710,184
			5.85%	5/1/2017	260,699	754,069
			5.85%	5/1/2018	243,723	761,277
			5.90%	5/1/2019	227,880	780,029
			5.90%	5/1/2020	212,688	784,349
			5.90%	5/1/2021	201,294	798,829
			5.90%	5/1/2022	189,900	810,100
				<u>\$ 2,437,230</u>	<u>\$ 7,247,018</u>	

Note: Bonds of this issue maturing on or after May 1, 2009 are subject to redemption prior to maturity at the option of the Issuer in multiples of \$5,000 in such order as the Issuer may determine, by lot within any maturity, on any May 1, and November 1 occurring on or after May 1, 2008, at the redemption prices (expressed as percentages of the Appreciated Amount on the date of redemption) set forth in the following table:

Redemption Period	Redemption Price
May 1, 2008 through April 30, 2009	103.0%
May 1, 2009 through April 30, 2010	102.0%
May 1, 2010 through April 30, 2011	101.0%
May 1, 2011 and thereafter	100.0%

Mandatory Redemption

The Bonds maturing on May 1, 2018 are term bonds subject to mandatory redemption, in part by lot on the redemption dates and at a redemption price equal to the appreciated amount thereof, without premium, as set forth below:

Redemption Date	Appreciated Amount
May 1, 2015	\$ 933,679
May 1, 2016	\$ 975,733
May 1, 2017	\$ 1,014,768
May 1, 2018 (maturity)	\$ 1,005,000

The Bonds maturing on May 1, 2022 are term bonds subject to mandatory redemption, in part by lot on the redemption dates and at a redemption price equal to the appreciated amount thereof, without premium, as set forth below:

Redemption Date	Appreciated Amount
May 1, 2019	\$ 1,007,909
May 1, 2020	\$ 977,037
May 1, 2021	\$ 1,000,123
May 1, 2022 (maturity)	\$ 1,000,000

PELLSTON PUBLIC SCHOOLS

SCHEDULE OF INDEBTEDNESS

JUNE 30, 2006

	<u>Date of Note</u>	<u>Amount of Note</u>	<u>Interest Rate</u>	<u>Date of Maturity</u>	<u>Total Outstanding at June 30, 2006</u>	<u>Total Interest Payable</u>
1992 General Obligation Capital Appreciation Bonds	11/19/92	\$ 2,894,928	6.80%	5/1/2007	<u>\$ 186,444</u>	<u>\$ 303,555</u>

Note: Bonds of this issue maturing on or after May 1, 2003 are subject to redemption prior to maturity at the option of the Issuer in multiples of \$5,000 in such order as the Issuer may determine, by lot within any maturity, on any May 1, and November 1 occurring on or after May 1, 2007, at the redemption prices set forth in the following table:

<u>Redemption Period</u>	<u>Redemption Price</u>
May 1, 2007 through April 30, 2008	103.0%
May 1, 2008 through April 30, 2009	102.0%
May 1, 2009 through April 30, 2010	101.0%
May 1, 2010 and thereafter	100.0%

PELLSTON PUBLIC SCHOOLS

SCHEDULE OF INDEBTEDNESS

JUNE 30, 2006

	<u>Date of Note</u>	<u>Amount of Note</u>	<u>Interest Rate</u>	<u>Date of Maturity</u>	<u>Total Outstanding at June 30, 2006</u>	<u>Total Interest Payable</u>
2004 Energy Conservation Improvement Bonds	7/9/2004	\$ 575,000	4.21%	11/1/2006	\$ -	\$ 11,157
			4.21%	5/1/2007	50,000	11,157
			4.21%	11/1/2007	-	10,104
			4.21%	5/1/2008	50,000	10,104
			4.21%	11/1/2008	-	9,052
			4.21%	5/1/2009	55,000	9,052
			4.21%	11/1/2009	-	7,894
			4.21%	5/1/2010	55,000	7,894
			4.21%	11/1/2010	-	6,736
			4.21%	5/1/2011	60,000	6,736
			4.21%	11/1/2011	-	5,473
			4.21%	5/1/2012	60,000	5,473
			4.21%	11/1/2012	-	4,210
			4.21%	5/1/2013	65,000	4,210
			4.21%	11/1/2013	-	2,842
			4.21%	5/1/2014	65,000	2,842
			4.21%	11/1/2014	-	1,474
			4.21%	5/1/2015	70,000	1,474
				<u>\$ 530,000</u>	<u>\$ 117,884</u>	

Note: This Bond is not subject to redemption prior to maturity by the District.

PELLSTON PUBLIC SCHOOLS

SCHEDULE OF INDEBTEDNESS

JUNE 30, 2006

	Date of Note	Amount of Note	Interest Rate	Date of Maturity	Total Outstanding at June 30, 2006	Total Interest Payable
Durant Settlement Bonds	11/24/1998	\$ 43,640	4.76%	5/1/2007	\$ 2,212	\$ 852
			4.76%	5/1/2008	2,318	747
			4.76%	5/1/2009	10,310	4,151
			4.76%	5/1/2010	2,546	520
			4.76%	5/1/2011	2,665	399
			4.76%	5/1/2012	2,792	272
			4.76%	5/1/2013	2,925	139

Note: This Bond is not subject to redemption prior to maturity by the District.

PELLSTON PUBLIC SCHOOLS

SCHEDULE OF INDEBTEDNESS

JUNE 30, 2006

	<u>Date of Note</u>	<u>Amount of Note</u>	<u>Interest Rate</u>	<u>Date of Maturity</u>	<u>Total Outstanding at June 30, 2006</u>	<u>Total Interest Payable</u>
Bus notes payable						
2004 bus note payable	10/8/2004	\$ 54,110	3.04%	9/22/2006	\$ 10,822	\$ 1,316
			3.04%	9/22/2007	10,822	987
			3.04%	9/22/2008	10,822	658
			3.04%	9/22/2009	10,822	329
					<u>43,288</u>	<u>3,290</u>
2003 bus note payable	8/19/2003	53,102	2.87%	8/19/2006	10,612	940
			2.87%	8/19/2007	10,916	636
			2.87%	8/19/2008	11,230	322
					<u>32,758</u>	<u>1,898</u>
2002 bus note payable	7/16/2002	50,000	3.88%	7/16/2006	10,373	821
			3.88%	7/16/2007	10,775	418
					<u>21,148</u>	<u>1,239</u>
2001 bus note payable	8/30/2001	53,936	3.68%	8/30/2006	<u>11,581</u>	<u>426</u>
Total bus notes payable					<u><u>\$ 108,775</u></u>	<u><u>\$ 6,853</u></u>



**INDEPENDENT AUDITORS' REPORT ON INTERNAL
CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT
OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

July 21, 2006

Board of Education
Pellston Public Schools
Pellston, Michigan

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of ***Pellston Public Schools*** (the "District") as of and for the year ended June 30, 2006, and have issued our report thereon dated July 21, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted a matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the District's ability to initiate, record, process, and report financial data consistent with the assertions of management in the financial statements.

The reportable condition is described as follows:

Due to staff size, there is limited segregation of duties over cash receipts and disbursements and the recording of these transactions. The District recognizes this risk, but no change will be implemented because the costs would exceed the benefits.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable condition described above is not a material weakness.

Compliance and other matters

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the audit committee, management, others within the organization, and the Board of Education and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink, reading "Lehmann Johnson". The signature is written in a cursive, flowing style.



REHMANN ROBSON

Certified Public Accountants

A member of THE REHMANN GROUP

An Independent Member of Baker Tilly International

July 21, 2006

Superintendent and Members of
The Board of Education
Pellston Public Schools
Pellston, MI

Through our role in performing financial statement services for the past three years, we have become familiar with your systems, operations and management team. As we work with our clients, we strive to provide direction and constructive feedback to help facilitate their success. The better we get to know you and your objectives, the more we can offer in terms of proactive advice.

In planning and performing our audit of the financial statements of ***Pellston Public Schools*** for the year ended June 30, 2006 we considered the District's internal control structure to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control structure.

However, during the above-mentioned engagement, we became aware of certain informational matters. The memorandum that accompanies this letter summarizes our comments and suggestions regarding these matters. This letter does not affect our report dated July 21, 2006 on the financial statements of ***Pellston Public Schools***.

We have already discussed these comments with the Superintendent, and we would be pleased to discuss them in further detail at your convenience.

If we can be of assistance, we hope you will view us as an integral part of your team.

Best wishes for a successful 2006-2007.

Encl.1

PELLSTON PUBLIC SCHOOLS
COMMENTS AND RECOMMENDATIONS
JUNE 30, 2006

PURCHASING OF SUPPLIES AND EQUIPMENT

The State of Michigan, Department of Education requires that competitive bids must be obtained for remodeling, procurement of supplies, materials and equipment for items above a limit established in Sections 623a, 1267 and 1274 of the Revised School Code. The base established for 2005-2006 fiscal year is \$18,915. In our testing of the purchases of the Pellston Schools we noted that a block of computers purchased exceeded the \$18,915, after adding additional hardware and shipping. Price quotes were received prior to the purchase however; no documentation was retained. We recommend that as the school district works to revise its current policies that the competitive bidding requirements of the State are incorporated into the policy and that the school follows the policy.

COMPUTER SECURITY

Recognizing that computers are an integral part of the curriculum and reporting of the school district, it is important to maintain the security of the systems and information. In our discussions with management, we noted that passwords are not changed on regular intervals. Because password security is an important control, we recommend that the school district review the password controls on all computers and consider implementing a periodic requirement for changing of passwords, with appropriate monitoring.

ATHLETIC EVENTS AND OTHER FUNDRAISING ACTIVITIES

Verifying cash

The school district operates in a fiduciary role for many fundraising activities. Considerable cash is collected in certain fund raising activities and also at athletic events. When cash is turned into the central office, it is recounted and a receipt generated, although not always immediately.

At athletic events, concession stands and other functions where larger volumes of cash are handled, two people should witness and verify the final counting and reconciliation of cash and sign a form indicating such.

Referee payments

The current practice for payment of referees is to issue checks in advance of the activity and pay them prior to service. Checks are often issued to the "team leader" who then pays the other officials. Frequently the checks are cashed in the cash box of the event. The IRS requires that all businesses report distributions of over \$600 per year on a form 1099. All other contractors and employees of the school district are paid after the completion of the service. By generating the checks in advance there are frequently many voided checks due to weather or change in officials. Therefore, we recommend the following:

That the athletic director prepares and approves a voucher for each referee or official individually to be paid for after the event is concluded. The checks will be issued after the event and when the disbursements clerk has the tax identification numbers of the official, in the normal payment cycle.

STATE CHART OF ACCOUNTS

The school district does not follow the state chart of accounts for its account numbering system, which requires a second set of numbers to be maintained. In an effort to better comply with the requirements of the state, the school district should work toward changing the numbering system to more closely follow the state requirements.

The school district does not maintain a GASB 34 fund to record the government-wide financial statement entries necessary. The school district may want to consider maintaining this fund.

MICHIGAN FINANCE QUALIFYING STATEMENT

All governmental units subject to the Revised Municipal Finance Act (PA 34 of 2001) must submit their qualifying statement electronically using the Department of Treasury's website. The District must establish a password to submit the qualifying statement on-line. If necessary, the Business Manager or Superintendent must call the Local Audit and Finance Division of the Department of Treasury (517) 373-0660 and request one.

ELECTRONICALLY FILING THE FINANCIAL STATEMENTS

Beginning with the fiscal year ended June 30, 2005, the District may submit their financial statements to the State of Michigan electronically. To do so, the financial statements must be created electronically in an Adobe Acrobat file. This file may be forwarded to bond counsel for preparation of the SEC continuing disclosures. We would be happy to provide an electronic version of the financial statements for your use.

CONCLUSION

It has been a pleasure to provide audit services to *Pellston Public Schools*. Management was well prepared for the audit, providing us with all requested information.

We appreciate your business! Thank you.